



POLICE AND FIRE RETIREMENT SYSTEM OF SPRINGFIELD, MO

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Minutes March 10, 2010

1. Call to Order

Hoffman called the meeting to order at 6:05 p.m. Minutes taken by White.

Attendance

Members	Representation	Present	Absent
Ken Homan	Chairman	X	
Beau Barrett	Citizen		X
David Carter	Fire	X	
Jim Edwards	Police	X	
Ron Hoffman	Retiree	X	
Brady Stark	Police	X	
Chris Thompson	Fire	X	
Mary Mannix-Decker (NV)	Finance		X
Cindy Rushefsky (NV)	City Council Liaison	X	
Dan Wichmer (NV)	Law		X
Nikki White (NV)	Secretary	X	

NV = Non-voting

John Bishop, Charlie Cowherd and Joshua Hartman were also present. They will be sworn in at the end of March as new members of the Pension Board.

2. Quarterly Investment Report – Gino Reina, Segal Advisors

Reina passed out copies of the Analysis of Investment Performance through December 31, 2009 (copy on file).

Financial Market Conditions: Review of Fourth Quarter 2009

Reina stated that Gross Domestic Product increased at a 5.7 percent annualized rate. This number has been recently revised to 5.9 percent. This is the second consecutive quarter of GDP increase following four pretty negative quarters. What drove GDP during the fourth quarter is inventory buildup in terms of corporate America. To a smaller degree the impact on the government stimulus as it relates to GDP was fairly minimal. There was a pickup in personal consumption accounted for by 1.4 percent of GDP. Overall not too much happened in the fourth quarter.

Over the last 12 months we have seen a small amount of inflation in the neighborhood of two to three percent. This is along the normal averages related to CPI. The increase in CPI can be attributed to energy, which increased by 19 percent year over year. The fed funds target rate remained at zero percent through

the end of December 2009. What we are seeing now is a large disparity in terms of what the fed will do in 2010. Unemployment will remain in the 9-10 percent area throughout 2010. The big challenge with the fed is not to fall back into a double dip recession. The unemployment rate at year end was 10.1 percent. Reina said it will probably take five to six years to get back to a five percent unemployment rate. There are many individuals who are working part-time who wish they were working full-time and are not reflected in the unemployment rate. If those people are taken into consideration it brings the number to nearly 17 percent.

The S&P 500 for the quarter was up six percent, up 26.5 percent for the year. However, it is important to remember the stock market was down 38 percent. For the 10-year period the S&P 500 is down one percent per year. People who had all their money in stocks lost about 10 percent over the decade. This is comparable to the 1930's during the Great Depression era. Russell 1000 Growth was up 37.2 percent for the year and Russell 1000 Value was up 19.7 percent for the year. The main culprit for the large disparity really comes down to the Value benchmark having a lot of financials. The story of how the banks did doesn't need to be retold. The MSCI EAFE was up 31.8 percent for the year. So internationally the market did better relative to the U.S. The MSCI EM was up 78.5 percent and for a 10-year period was up 9.8 per year.

On the fixed income side, Barclays Capital Aggregate (investment grade bonds) was up 5.9 percent for the year. In 2008, the only positive returns were from U.S. treasuries. In 2009, the only negative returns were from U.S. treasuries. In the bond world, for the most part everything that went down in 2008 made up their losses in 2009. That cycle is typically four to five years. The area that got hit the hardest was high yields. Citigroup Non-U.S. WGBI was up 4.4 percent for the year. HFN HFOF Multi-Strategy (hedge funds) was up 9.7 percent for the year. Commercial real estate was down 16.9 percent for the year.

Reina said on the commercial real estate side he expects to see a pickup in the second half of 2010 and into 2011. Commercial real estate has only been going down for 18 months unlike residential real estate which has been going down for nearly four years. We are currently seeing the residential side bottoming out. Commercial mortgage backed securities haven't fully come back yet. He thinks in the first half of 2010 the market will figure this out. Segal is advising their clients, if they want to take an opportunistic stance with real estate after the declines that have been seen, they might want to start putting money toward commercial real estate sometime toward the end of the year or beginning of 2011. They want to see the commercial backed security issue play out a little more.

In December 2009 the National Federation of Independent Business (NFIB) Small Business Confidence Index fell to 88, the lowest level since July 2009. According to the organization's Small Business Economic Trends Survey, business optimism remains dim. Small businesses represent 99.7 percent of all employer firms and have generated 64 percent of the net new jobs created over the last 15 years. Healthcare is a major issue that will affect this area. As far as bank lending, credit conditions continue to make a slow recovery to normalcy. As the access to credit increases, economic growth may begin to expand; however, growth will continue to sputter without free flow of credit between lenders and borrowers.

Net debt as a percent of GDP for major advanced economies has steadily increased since 2007. The U.S. in 2007 was a bit under 50 percent and as of 2010 it will be in the 70 percent area. Italy and Japan will be over 100 percent. Germany and France will be in the 70 percent area and Canada will be just over 25 percent.

Homan entered and welcomed the new members. He stated that the board and investment subcommittee have a lot of work ahead of them. This plan can certainly not withstand another bear market with the current investment strategy. Several other options are available and will need to be researched. The closing of the plan will certainly affect the investment strategy. He apologized for not being able to attend the entire meeting due to his presence being needed at the citizen's task force meeting.

Springfield Police Officers & Firefighters Quarterly Investment Report

Reina reviewed the following investment managers' information with the new members.

<u>Investment Manager</u>	<u>Mandate</u>	<u>Benchmark</u>
State Street Global	All Cap Equity	DJ Wilshire 500
Pictet Asset Management	International Core	MSCI EAFE Net +3%
Galliard Capital Management	Fixed Income Intermediate	Barclays Capital US Govt/Credit Inter.
Brandywine Global	Fixed Income International	Citigroup World Gov't Bond ex-US +3%
Prudential Real Estate	Real Estate	NCREIF National

As of September 30, 2009 the plan had \$118,505,046 and it increased to \$129,432,309 as of December 31, 2009. In terms of asset allocation, we are little underweight on the equity side. The target is 40 percent and the plan is at 36.87 percent. The bond segment is a little overweight at 26.79 percent with a target of 21.75 percent. This is due to the board electing to deposit the telecom settlement funds in to the bond segment which put it overweight. International equity is at 19.13 percent which is in line with its target of 20 percent. International fixed income is slightly overweight at 12 percent with a target of 10.75. Real estate is currently at 5.21 percent with a target of 7.5 percent.

Gain/Loss Summary

<u>Composite</u>	<u>Quarter</u>	<u>YTD</u>
Beginning Market Value	118,505,046	98,796,512
Net Contributions	7,928,462	12,487,841
Fees/Expenses	(36,697)	(87,299)
Income	353,782	1,344,233
Gain/Loss	2,681,616	16,890,933
Ending Market Value	129,432,209	129,432,209

For the quarter, the plan returned 2.39 percent which is slightly behind the policy index of 2.60. For July 2009 to December 2009 the return was 14.15 percent which is line with the policy index of 14.27 percent. Year-to-date the plan is up 17.90 percent. The three-year performance is -2.72 percent compared to the policy index of -0.83. Since inception on April 1, 2005, the plan is up 1.44 percent compared to the policy index of 2.48 percent.

On the equity side, State Street Global's performance had an increase of 28.75 percent year-to-date. Their benchmark is 29.42 percent. Pictet (international equity) had a very difficult 2008. They did bounce back to a certain degree and are up 41.23 percent compared to the benchmark of 35.73 percent. Pictet uses MSCI NET EAFE +3% as a benchmark. Pictet agreed to the +3% when the board hired them so they do have some ground to make up. They did place in the top 17 percent of all international equity managers.

Homan asked Reina to explain to the new members what the policy index is composed of and how often the policy index is adjusted to the actual asset allocation in the plan. Reina said that the policy index is the target allocation. On page 32 there is a history of the policy index. When Segal was first hired the

allocation was 50 percent stocks (Barclays Capital Intermediate US Government/Credit) and 50 percent S&P 500 Index. In April of 2007, the plan became more diversified with 25.50 percent Barclays, 43.75 percent Wilshire 5000 Total Market Index, 20 percent MSCI EAFE NET +3%, and 10.75 percent Citi WGBI x US +3%. In September of 2007, the current allocation was implemented. Homan stated that these are the most important comparisons you're going to find in terms of whether the managers are doing their jobs and accomplishing what the plan is supposed to. Those who might be critical of the investments need have their attention drawn to these numbers. Reina added that at the end of the day if the stock market was down one percent per year for ten years then there weren't a lot of places to make money. This plan has a 7.5 percent return assumption. The only way that would have been accomplished would have been if you knew 10 years ago what was going to happen and had a bunch of money in emerging markets and more money in real estate starting in 2000, which would have been a tough game. Long term you want to outperform the policy index. It not only shows whether the managers are doing their job, but also if the asset allocation makes sense.

Galliard outperformed their index with a 14.53 percent compared to the benchmark of 5.24 percent. They are in the top 10 percent of fixed income managers. Since the board hired them they are up 8.24 percent compared to the benchmark of 5.93 percent. They are subsidiary of Wells Fargo and they only do fixed income. Brandywine is up 10.28 percent for the year compared to the benchmark of 7.49. Since their inception into the plan, they are up 7.60 percent compared to the benchmark of 12.04 percent. PRISA is the real estate allocation which intended to be a long-term investment. The most recent time period has not been very comforting however. Since inception in October of 2007, they are down 21.30 percent compared to the benchmark of -18.21 percent. Year-to-date they are down 34.24 percent compared to the benchmark of -30.57 percent. Segal has about 15 clients who are using PRISA. The board hired them because they have been doing institutional core real estate investing since the 1970's. Reina added that as a side note, the one thing that hurt PRISA was forward commitments. Reina said that one thing he can say with certainty is that PRISA has been very aggressive with writing down their portfolio. They expect when valuations start to return, these unrealized losses of -34.24 percent will bounce back much quicker relative to the benchmark. Reina said that over the long term everything should work out nicely. From a liquidity standpoint, we put in a redemption request for the entire \$6.7 million. Unfortunately you can't get your money out so they noted that in 2010 they will not be satisfying any withdrawal requests. However, starting on June 30, 2010 they will be distributing cash flows. At the high point, Prudential had about \$1.3 billion in withdrawal requests. More recently that number has gone down to under \$1 billion. Their clients have changed their minds on taking the money back.

This concluded Reina's quarterly investment report.

3. Asset Liability Modeling

Reina said that the sales tax and the closing of the plan haven't definitely changed things to say the least. The closing of the plan totally changes the dynamics of the plan. When something like this happens, his firm recommends Asset Liability Modeling. This is a six to nine month process where you model out the liabilities, model out the contributions and cash flow coming in, and figure out what portfolio is best suited for that situation. It is a probabilistic study. What they are doing is saying that if you do "x" asset allocation with this contribution flow and this liability structure, then this is the probability of what your plan will look like 5, 10 and 20 years from now.

Reina distributed a presentation titled "Asset Liability Modeling (ALM) – A Tool for Managing Funding Volatility". (On file)

Two of the objectives are to review the key risks in the liability structure and review the asset allocation policy. This will include estimating the expected rate of return and showing the impact of the asset allocation including contribution rate, funding ratio and solvency ratio. They will run 2000 scenarios and they will say where the funding ratio will be 10 years from now. He said this is a tool that is needed to make informed decisions.

Hoffman stated that with the way the sales tax was marketed the board is going to have to be very careful about future investing. The discussion of the plan being closed to new members wasn't really marketed as a part of the tax. He's afraid if a more conservative investment strategy is utilized then the funded ratio won't be as high as some people might expect. This could affect the outcome a very much needed renewal of the sales tax in five years. Reina said that if a more conservative approach is taken based on the plan being closed and making sure the liabilities are met then yes, there will be lower returns. He added that as a board, this might be the right thing to do. However, what if the equity market rebounds and returns 15 percent a year for the next five years and this plan returns six percent. Hoffman said that's a problem because we need the tax to renew again and we've kind of trapped ourselves. Reina confirmed that most of the plan's gains have been realized by the equity market. When things are reallocated he's said equities wouldn't go to zero, but they definitely wouldn't stay at 60 percent.

Carter said that this study sounds like exactly what is needed because as a part of those 2000 scenarios you could see the results of a five-year tax versus a 10-year tax. Reina said absolutely. This report will help determine which worst case scenario is more palatable based on your asset allocation. It will also show you that there's a five percent chance or a ten percent chance of these bad things happening just because of what you're invested in. The question is, are you comfortable with that downside?

Bishop asked if the board has established a target funding ratio. Rushefsky said no, that is something that needs to be determined. Bishop added that he thinks the board needs a three, a five and a 10-year goal. Edwards added that with the plan being closed, the day that the last active employee retires this fund had better be at 100 percent. Otherwise the City will have to cover the shortage. Reina added that the ALM study will assist in determining these goals and what is a reasonable funding target.

Reina stated that the study will cost around \$60,000. There will be a tremendous amount of work on their end as well as the board's. It will also require several meetings. Segal will work with the actuary as well as the City to gather the necessary information to begin the process. Carter asked if charges from the actuary were to be expected. Reina said that he hasn't typically seen any extra cost from the actuary for providing the data. Reina said Segal has done over 100 ALM studies.

Rushefsky asked Reina why the board would be paying extra for this. She thought this would have been something that his firm would do anyway. Reina said that the ALM study is not for everyone. Not everyone has to do one so when Segal presented their initial proposal it was based on the fact that an ALM study would not be necessary. Otherwise their yearly fee would have been much higher. He thinks this is a fair fee considering the work that is involved. Carter asked if the need to do this is more correlated to influx of revenue from the sales tax, or the closing of the plan. Reina said in isolation he would say yes, in combination he would say absolutely. If you close the plan and have increased revenue, you need to do an ALM study. After the initial study is complete, it is updated typically every five years. However, the cost will not be \$60,000 because the initial data is already complete.

4. Adjournment

The meeting was adjourned at 8:20 p.m. on March 10, 2010.